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CENTRAL INTELLIGENCE AGENCY  
OFFICE OF CURRENT INTELLIGENCE  
6 June 1955

State Dept. review completed

TO: Deputy Director (Intelligence)

SUBJECT: The Forthcoming US-South Korean Talks

NSA review completed

A South Korean economic-military mission is now in the United States for discussions promised last March by FOA director Stassen. The negotiations, which will start about 20 June, were intended originally to cover only the perennial exchange rate problem, but it is apparent that President Rhee intends to use the opportunity to revive all his old grievances, including demands for a major share of Asian aid, an increased military establishment, termination of the armistice, and a stop to the "build-up" of Japan.

The preparations being made by Rhee suggest that he will not retreat readily, and the negotiations are likely to bring South Korean-US relations to an all-time low. In order to prepare both domestic and foreign opinion, he is renewing his familiar tactics of "spontaneous" demonstrations, attacking the United States and Japan in his controlled press, and falsely attributing "promises" to American officials. He has reportedly instructed his diplomatic missions in Washington, New York, and Tokyo to "promulgate widely" his objectives.

The adoption of a realistic exchange rate, and related issues, such as the adequate pricing of imported aid goods, budgetary and tax reform, and the proper use of Korea's own foreign exchange, will constitute the crux of the talks. Rhee intends not only to set a rate for the South Korean hwan far below its realistic level, but to make it "permanent." He maintains a peculiar theory, which has become an obsession, that changes in the exchange rate cause inflation, rather than reflect inflation.

Even if a realistic rate could be agreed on in the beginning, the continuing inflation would make such a pegged rate progressively more costly for the US, aid goods would be underpriced, thus minimizing their counterinflationary effect, black markets would be stimulated, and favorites would gain windfall profits (which would be partly diverted to Rhee's Liberal Party). Economic Co-ordinator Wood has recommended that the US face the issue on its merits, refuse to agree to a fixed rate, and be prepared for the acrimonious controversy that is bound to ensue.

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[redacted] Rhee also plans to demand a minimum 900 million dollar military and economic aid program for fiscal 1956--an increase of 200 million dollars over the 1955 level. The United States plans to allocate \$628 million, of which \$280 million is economic aid. In view of Rhee's vigorous press campaign that last year's aid was "inadequate," the planned reduction will be an inflammatory issue, which the US hopes to keep out of the discussions.

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Rhee is also reported planning to demand that the United States increase the South Korean military establishment (which is already larger than Korean manpower resources can properly support), or withdraw the UN Command from Korea. This demand is in line with Rhee's overriding objective of unifying Korea under his leadership, which he believes can be done only by military force. By maintaining the second largest non-Communist army in the world, Rhee would be in a position to exploit any opportunity to achieve this objective. It also would enable him to exercise a disproportionate influence in Far Eastern affairs, keep the US stake in Korea high, uphold Korea's prestige, and provide security.

General Taylor (CINCUNC) has recommended that Rhee be informed during the discussions that the US plans a reduction of South Korean forces. Ambassador Lacy has recommended strongly to the contrary, believing that the talks would be jeopardized by the introduction of this subject, and that domestic and international political considerations mitigate against such action at this time.

The negotiations give promise of being a repetition of last summer's talks, when Rhee delayed implementation of the aid program for four months. If he follows his usual negotiating techniques, the following can be expected: (1) Having no legitimate bargaining position, he will create one by getting the pot boiling on as many issues as possible, and then bargain against promise of good behavior (this tactic is already under way); (2) revive all his old demands, ignoring whatever has been previously granted to him to "settle" those demands; (3) remain adamant, believing that American impatience will lead to concessions; and (4) toss in new demands whenever agreement has apparently been reached. He can also be expected, as was the case last year, to ignore or circumvent provisions of any final agreement which are distasteful to him.

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